DOW THEORY LETTERS INC.

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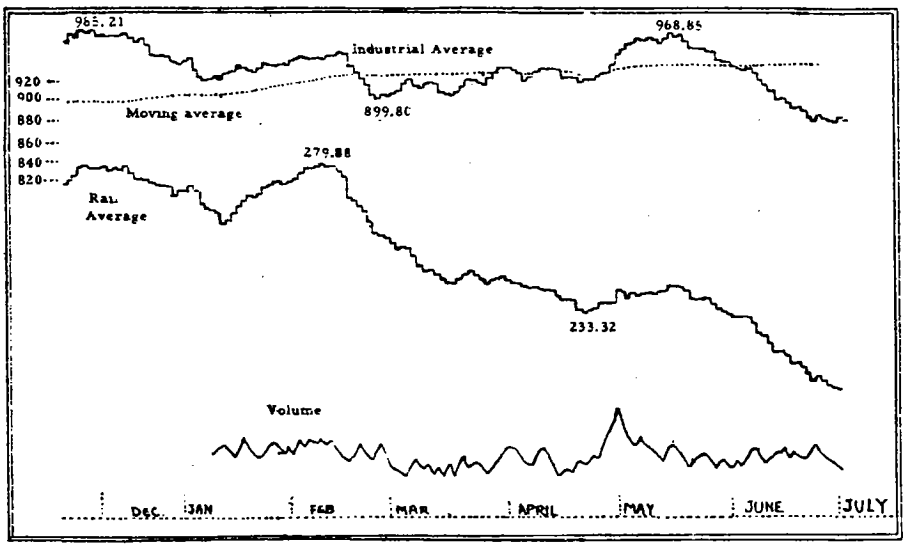
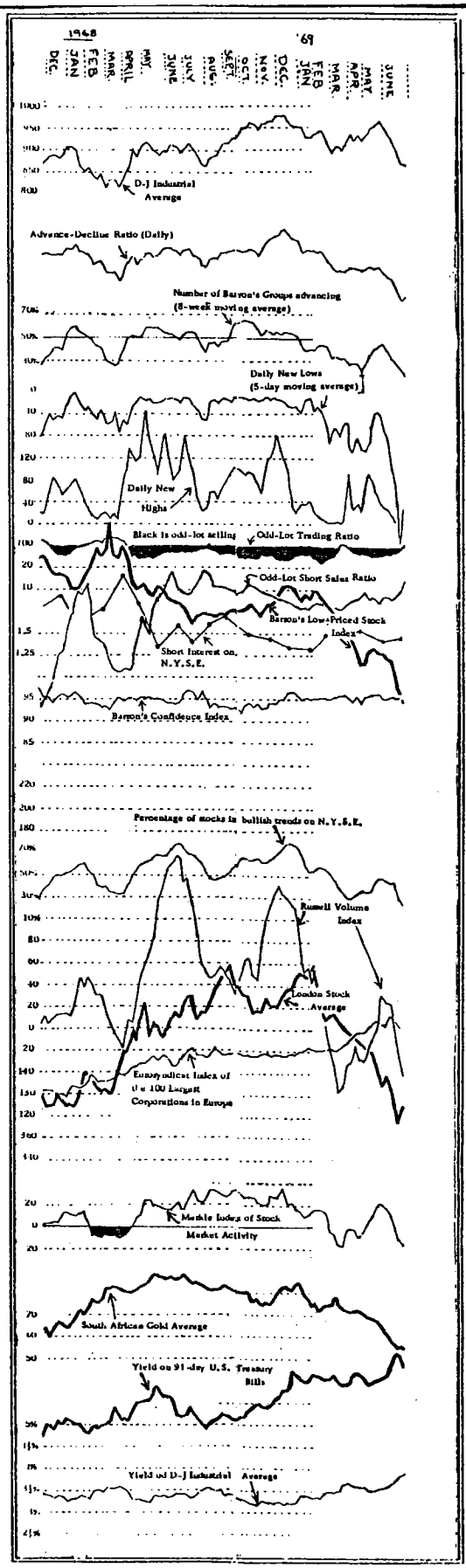
THE MARKET: Late in the 1932-37 bull market business expanded from the depths of the early '30' Depression years. Questioned about this "mircle," President Roosevelt retorted confidently, "We planned it that way." A year later, following the 1937 stock market and business smash, those words came back to haunt him. "Did you plan this mess too, Mr. President?" were the words on every businessman's lips. From the White House came silence.

I could not help thinking of that incident when I read this in a column written a few weeks ago by nationally-syndicated columnist Sylvia Porter, a woman with many pipelines in Washington: "If you have been taking a grim bearing in the stock market, you won't get much sympathy at the White House or the headquarters of the Federal Reserve System. Since Washington's objective above all others now is to kill the psychology of inflation, neither administration nor Federal Reserve officials are at all unhappy about the recent sharp decline in the market...." So I suppose you could say that Washington has planned it that way.

Figuring from the May high on the Dow Industrials (968.85), the senior Average has dropped a straight 100 points without producing anything resembling an upward correction. The Advance-Decline Ratio has been down on 27 out of the last 31 days, which is absolutely extraordinary in itself. Based on any "normal" reckoning, this market is heavily oversold, and some sort of rally should be in order. But the primary trend is a law unto itself, and each time the market establishes a new record it merely means that a previous record has been surpassed.

Readers of these Letters, I trust, are not wringing their hands as they wait for the long overdue rally. They have been out and on the sidelines, and the appearance or absence of a rally at this time is merely a situation of academic interest.




1968
'69
D-J Industrial Average
Advance-Decline Ratio (Daily)
Number of Barron's Groups advancing (8-week moving average)
Daily New Lows (5-day moving average)
Daily New Highs
Black is odd-lot selling
Odd-Lot Trading Ratio
Odd-Lot Short Sales Ratio
Barron's Low-Priced Stock Index
Short Interest on N.Y.S.E.
Barron's Confidence Index
Percentage of stocks in bullish trends on N.Y.S.E.
Russell Volume Index
London Stock Average
Eurosyndicat Index of the 100 Largest Corporations in Europe
Merkle Index of Stock Market Activity
South African Gold Average
Yield on 91-day U.S. Treasury Bills
Yield on D-J Industrial Average

 Here are some current observations which I find of interest. At no time has the 100 point decline verged on panic. The drop has been orderly, based more on a lack of buyers than on any massive entrance of sellers. Thus, Exchange volume since the May peak has never expanded dramatically on the downside. I want to stress, however, that most important primary declines do attract real selling pressure before they are over.

Odd-lotters have moved to the buy side of the market which is normal as a market declines ("lower prices are bargains"). But usually, prior to a true bottom, the odd-lotters switch to less buying or actual selling. Odd-lot short selling has never risen appreciably on this decline. Yet most major bottoms are accompanied by relatively high odd-lot short sales.

Attempts to rally, so far, have not attracted Rail buying. A laggard Rail Average is a definite minus during rallies (as would be a laggard Industrial Average). I might also mention that rallies in a primary bear market can be extremely erratic and deceptive. Often the market will not do "what it is supposed to do." Thus mild primary down-legs can be followed by explosive rallies, and extensive primary down-legs can be followed by weak rallies or sideways "lines."

Finally, according to the latest report (received today) by the authoritative Bolton-Tremblay Bank Credit Analyst, the monetary situation is still bearish. Quoting from editor Donald Storey, "The coincidence of an extremely ominous long-run money and credit environment with a rapidly contradicting cyclical credit structure raises the spectre of a financial debacle greater than anything we have seen for many years."

CRYSTAL GAZING: Reading what the leading economists in the nation have to say is a most fascinating procedure these days. Never have there been more variables, never have so many had so much guessing to do.

Perhaps the biggest guess is whether the tight money policy or "crunch" of 1969 will result in any economic downturn. Some economists believe that the Federal Reserve Board is pursuing a fruitless policy and that inflation is here to stay, regardless of the cost or availability of money. Others believe that by the last quarter of 1969, we will be entering an economic recession.

The second question is, what will the Fed do next? If there is no slowdown in inflation, then it seems obvious to me that the Fed will "keep the screws on" the money situation. But if there is a recession, if unemployment mounts, what then? My opinion is that the Fed will tolerate "a mild recession," that they will be willing to hold the money line even if and when signs of a mild recession appear.

All very well, all very classical and academic. But there is another thought which occurs to me. What if the whole thing gets out of hand on the downside? What if sometime in 1969 we have a credit-panic together with mass liquidation amid skyrocketing interest rates. If that occurs, I personally doubt that the Fed will be able to handle the situation, and I doubt opening the money valves is going to immediately reverse the situation.

Then there is always the question of the stock market itself. An orderly decline without panic on Wall Street is acceptable and would obviously be welcomed by the Fed. But what about a full scale collapse, a smash which gets out of hand? It is well to remember that there are roughly 23 million stockholders today, and gauging what 23 million stockholders are going to do is a most difficult if not impossible task.

I also feel that almost all analyses these days are offered without thought to the direction of the primary trend. Most of the men writing today have spent their adult lives writing about the market and the economy while the primary trend of the market and the economy was bullish. Every recession, every market sell-off was ultimately followed by the great tide of the bull market. It was always a case of when or at what point the market and the economy would head up again.

But primary bear markets are different. In a primary bear market the prevailing overall trend is down, while the short-term (often manipulated trend) is up. During a bear market it is always a case of rallies providing hopes and holding action, but sooner or later the primary bear forces take everything down.

This is the thesis which today's analysts are not aware of. The broad sweep of events now is down, and the best laid plans will only provide pauses in the overall descent of the market and economy. This is indeed a pessimistic outlook, but I believe it represents reality.

Therefore, I urge subscribers not to place too much faith on what the analysts and business leaders hope for or predict. No man or group of men, no bank or treasury or group of central banks are powerful enough to reverse the fundamental

forces which are seeking to express themselves. Those forces are the forces of deflation and correction, and they have a 17-year bull market (1949 to 1966) to

I have emphasized this thesis of the primary trend, because I believe that it is of the utmost importance to subscribers to understand this principle. Conversely, a lack of comprehension of the primary concept will prove costly if not disastrous during the period ahead.

Speaking of crystal ball gazing, I am a little uneasy about the numerous predictions of "one of the greatest bond market rallies in history" coming up. One by one, the leading bond experts are coming forth with forecasts of a huge bond rally which will start as soon as the economy turns down. The thinking is so obvious that it bothers me. If a recession (brought on by tight money) begins, the Fed will quickly ease up on its monetary squeeze, thereby sending bonds flying skyward. The logic is irrefutable, if one bases everything on past action and performance.

But again there is one possibility that bothers me. Suppose the stock market does cave in, and suppose that a severe business recession begins. Corporate and personal income will then drop rapidly, perhaps precipitously. With it, tax receipts to the Government will decline sharply. In that case, the Treasury will be in dire need of cash to make up for the drop in tax receipts. This could mean a need for massive new Treasury debt issues, bonds, notes and bills. If tax receipts should drop off and the Treasury was then to come into the debt market for say $20 to $40 or more billions, the bond market would be faced with continuing chaos. I would not discount such a course of events.

Why are the bond experts not thinking along these lines, it might be asked? The answer (again) is that the experts are not thinking in terms of a major, primary bear market. It is obvious to me that already they are figuring in terms of a mild recession and then an economic pick-up as interest rates are eased. It ain't necessarily so.

THE PRIMARY TREND: I like very long-term charts. They tend to put the market into perspective in a way that no daily or weekly chart can do. Long-term charts are particularly useful in gauging the direction of the major or primary trend. I believe that this is a good time to take up some space (verbal and visual) with a discussion of two of my long-term charts.

In Letter 430 I drew particular attention to the 899.80 level on the Industrial Average. The 899.80 level, I stated, represented the last "stronghold" of the bullish argument. On June 12 Industrials closed below 899.80, thereby rendering an extremely bearish signal. The violation of 899.80 is now history, but what are the next check points to watch over the period ahead?

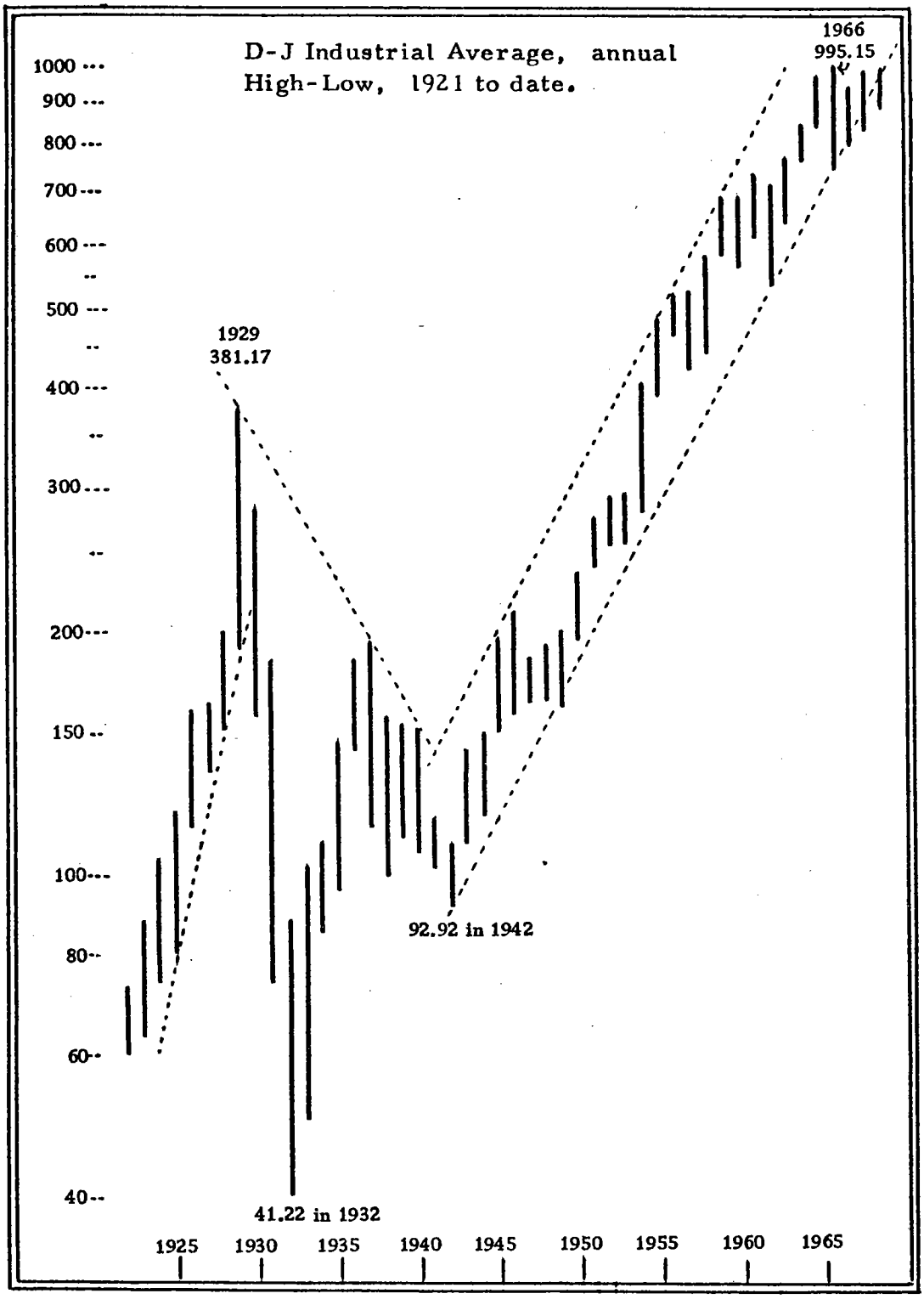
First, I will turn to the logarithmic bar-line chart, covering the annual high-low range of the Dow Industrials from 1932 to date. Note that a rising channel appears in the Dow from the low of 92.92 in 1942 to the present. The Dow has held within the limits of this channel from the low of 1942 to the high of 1966. This represents a period of 24 years, the longest channel in the history of the market.

As a rule, the longer a trendline or channel is respected, the greater the significance of an ultimate rupture of that trendline. The high and low for the Dow during 1967 was 943.08 and 786.41. Thus the year 1967 (even though its followed the 1966 bull market peak of 995.15) managed to hold within the channel. The 1968 low of 825.13 (see chart) did take the Dow below the lower limits of the channel, but the break was not decisive.

The last bar on the chart shows the upper and lower ranges for the Dow so far in 1969. At the 1969 high of 968.85, the Dow barely pushed inside the lower limits of the channel. At the current low the Dow is definitely below the lower limits of the channel. However, it seems to me that a decisive break below the channel would now entail a breaking of the 1968 low of 825.13. If 825.13 is violated, it will be the first time since 1966 that a preceding annual low has been penetrated. I therefore direct subscriber's attention to the 825.13 level as the place to watch on any further downside action from here. A violation of 825.13 it seems to me, would be ominously bearish.

The next chart (courtesy of Chartcraft, Larchmont, N.Y.) is a Point & Figure (P & F) chart of the Dow Industrials covering the period from 1929 to the present. This is a 10 point, 30 points reversal chart. This means that each box represents 10 points on the Dow. Only rallies and declines of 30 points or more show on the chart. The X's indicate rallies, the O's indicate declines.

To give an example of how this concentrated chart works , a rally from 500 to 525 back to 500 would not show on this chart, because the rally was less than 30 points. Obviously, a rally from 500 to 530 back to 500 would show on this chart since the rally covered a distance of 30 points on the upside and 30 points on the downside. Hourly

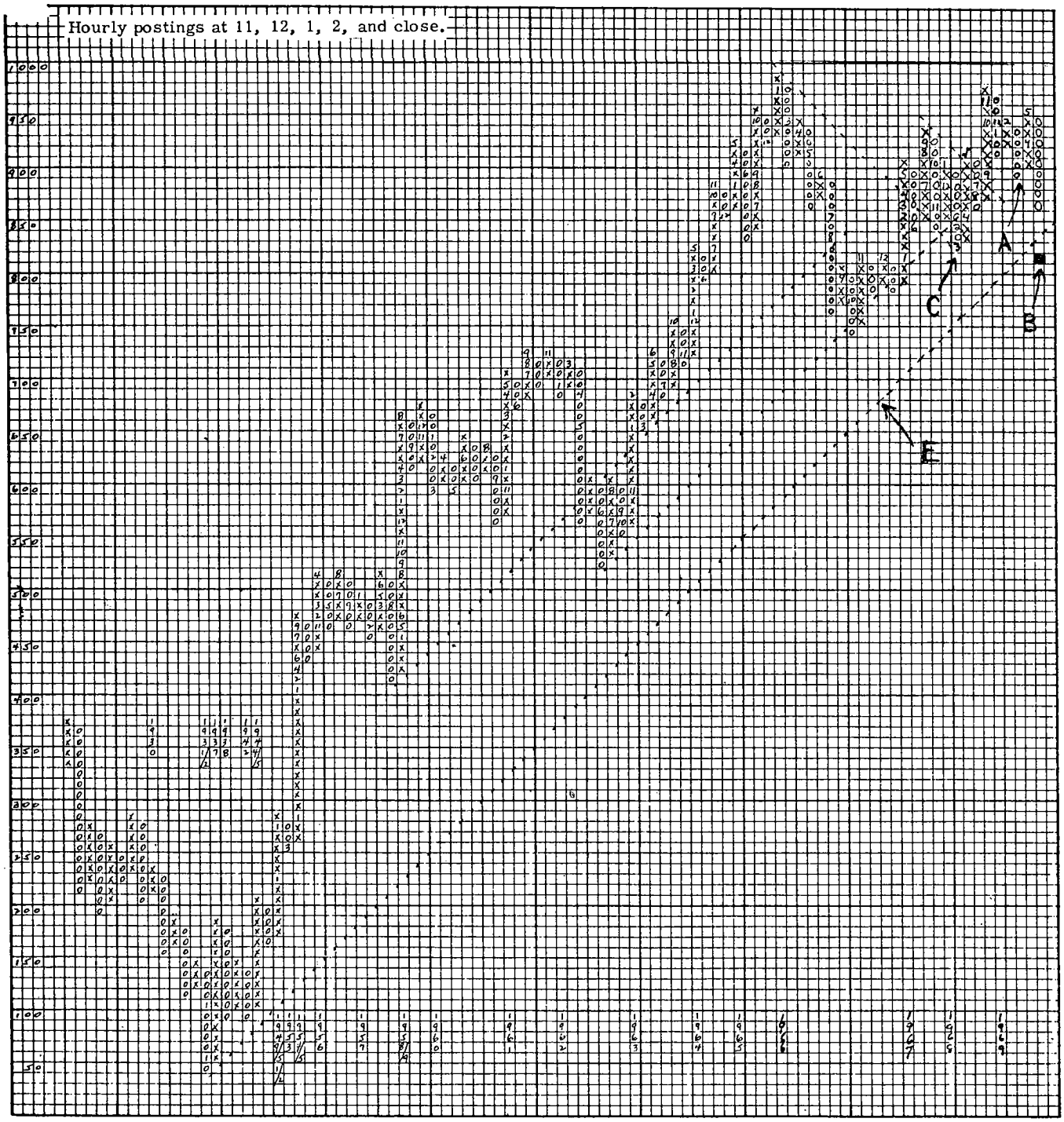


Dow figures posted on the tape at 11 A.M., 12 P.M., 1 P.M., 2 P.M. and the daily closing are used in constructing this chart.

I think it is significant that the 820 area (as was true on the annual bar-line chart) is also extremely important on the P & F chart. Note on this P & F chart that the Dow turned bearish at the 890 level, at which point it had broken below the previous low represented by the "O" at the 900 level (this preceding low at 900 marked "A" on the chart).

An even more important low than the 900 low is the Industrial low for the year 1968. The 1969 low occurred at 830 on the chart, and it is marked with a "C". Any forthcoming plunge by the Dow below the 830 level to 820 would

DOW - JONES INDUSTRIAL AVERAGE (10 x 30 points)



provide a doubly bearish P & F signal, since it would take the Dow below the 1968 low and also below the long-term trend-line marked "E" which extends back to the 1937 low! The all-important 820 box is shown on the chart by a solid black box marked "B".

CONCLUSION: Any closing below 825.13 on the annual bar-line chart would be extremely bearish. Confirming this, any hourly touching of 820.00 on the P & F chart would provide a most bearish signal. Thus I pick 820 as the next point on the downside to watch.

ODD & ENDS: Last week the 26-week U.S. Treasury bills set a yield record at 6.94 % thus approaching the time when a Treasury bill will yield 7% for the first instance in history.

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It isn't only the public and the amateurs who are getting hurt in this market. For instance, glance at this little clip form the June 28 issue of Bussiness Week.

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My two key Dow Industrial stocks are painting a picture of distribution. General Motors hit its high in 1965, as did DuPont. The latter is now at a seven year low. Other Dow stocks are taking a beating. Allied Chemical is at a 19 year low. Anaconda is at a four year low. International Harvester is at a five year low. Chrysler is at a three year low. United Aircraft is at a five year low.

A few private hedge funds are said to be in severe trouble—down as much as 40% even though they are theoretically supposed to make money by shorting in declines. They borrowed against unregistered stock that subsequently went down. Now the banks are angry, and the hedge funds can't sell their unregistered shares. Furious fund partners can't get out either, for the same reason.

VIETNAM "STRATEGY": In the June 14 issue of Business Week magazine the Nixon withdrawal strategy is examined. The policy of bringing the troops home is described as "irreversible." The Nixon strategy is admittedly a big gamble, and that gamble is predicated on three points.

(1) Saigon is supposed to respond with greater political and military effort. Saigon is to take up the slack. (2) The American people are to be patient with the slow-pull-out policy; they are not to put the pressure on. (3) Hanoi is supposed to read the troop withdrawal policy as a sign of strength, not weakness.

I believe that the Administration is going to be dead wrong on points 1 and 3, and possibly wrong on point 2. As for point 1, Hanoi has been fighting this war for 100 years, first against the Chinese, then against the French, now against the Americans. The American phase is very recent, and it is looked upon by Hanoi as just one more (and perhaps the final) phase in the take over of Vietnam. Because Hanoi has been fighting the war for decades and decades, it is, I think wishful thinking to believe they will "compromise" now. As for Saigon taking up the slack, I don't think they can do it. By most Americna accounts, the North Vietnamese fighters are superior to the soldier from the South.

(2) The American people may be patient for the next year or so, I don't know. As long as troops are being withdrawn, Nixon can probably keep the noise down. (3) As suggested in the point 1 answer, Hanoi will very definitely read the withdrawals as a sign of weakness. I can't imagine Hanoi signing a compromise peace while American troops are being systematically withdrawn.

Conclusion: The Nixon Vietnam policy is leading and heading for disaster. I don't think it's going to work on any count. The Administration is over the proverbial barrel, and I think they have now retreated into the world of fantasy, rather than face what is actually happening in Vietnam.

STOCKS: Bear markets can produce dramatic incidents, and here is one for the scrapbooks. The chart shows Anaconds, a Dow stock and one of the world's leading mining and fabricators, erasing half its market value in a period of 7 months. Part of this was in response to the nationalization of two of its Chilean mines, but part also was the force of the bear market. In a bull market I doubt if the same nationalization news would have taken Anaconda down half as far. (Anaconda chart courtesy of Traders Research, 101 Cherry St., Alton, Ill. 62002).